February 25, 2014

Co-Chair Paul R. Doyle

Co-Chair David A. Baram

Senator Kevin D. Witkos

Representative Dan Carter

General Law Committee:

I am submitting this testimony in opposition to HB 5260, AN ACT CONCERNING HEATING FUEL DELIVERY FEES, CHARGES AND SURCHARGES AND PREPAID GUARANTEED HEATING FUEL PRICE PLAN CONTRACTS.

<u>Overview:</u>

In response to the recent failing of a home heating fuel dealer in the State of Connecticut members of the legislature are proposing bills concerning pre-pay oil contracts. This failure resulted in customers, who have entered in to pre-paid fuel delivery arrangements, with no means to recuperate their payments. The state legislature is therefore attempting to enact legislation that will mitigate this risk in the future.

<u>Background:</u>

My company, F. F. Hitchcock Oil Co., LLC, located in Cheshire, is considered a young company in terms of heating oil dealers in the state of Connecticut. We have been delivering heating oil to our customers for only a period of five years and have only recently begun to deliver propane. In addition to our lack of age we are considered a smaller company, with an estimated 1.6 million gallons of delivered fuels for the 2013-2014 heating season. We are growing in size and delivered gallons, year after year, which is unusual in an industry where delivered gallons are shrinking due to increased equipment efficiency and diversified energy offerings.

<u>Special Pricing History:</u>

Our first season delivering fuel began with prices in the mid three dollar range and would see more than a 50% drop in retail pricing by mid-March of 2009 at which time we saw a dramatic increase in customers asking about various options to lock in their pricing for the 2009-2010 heating season. It was in the spring when we entered in to our first pre-paid fixed price contract with a customer. The customer happened to be a family friend who had recently received their income tax return. The previous year this customer was on a variable priced plan and experienced a wide range of fuel prices. With the money in hand and an uncertain oil market ahead this customer chose to lock in his price of fuel for the next year at $1.959 per gallon. As the following heating season moved along retail prices rebounded, with prices stabilizing in the mid two dollar range for the duration of the heating season. This customer's roughly $2000.00 investment saved him nearly $500 in potential higher fuel costs. This same customer has since remained with our company locking in his price in successive years at a savings. He locked in his price at $2.29 during the 2010-2011 heating season when prices rose from a low of $2.19 per gallon in July 2010 to $3.69 in mid April 2011. He has since locked in his price every year at a significant savings.

These savings have been shared by many customers during our short history offering pre-paid oil pricing. Pre-paid oil customers make up a very small percentage of our customers. This year we have only 40 customers on this plan representing approximately 30,000 gallons with an average locked in price in the $3.50 range. With temperatures being colder than usual, oil consumption therefore is higher than normal this heating season. Due to this, the majority of our pre-paid customers have used most of their agreed upon gallons leaving us with approximately 4,500 gallons outstanding. Our company maintains a bulk facility with 100,000 gallons of heating oil storage located in Cheshire, Connecticut. We use this storage in order to comply with current regulations regarding pre-paid heating oil. As we receive payment, we purchase the oil and have it delivered to our storage facility. We maintain at all times the remaining quantity to be delivered in our storage tanks.

<u>Special Pricing Benefits/Application:</u>

With such a small percentage of our customer base taking advantage of our pre-paid oil program a few questions usually come up:

1. **If a customer can save money every year, why don't more customers choose to participate in this program?** This question is more complicated than it seems. The first reason most customers choose not to participate in this program is the obvious up front financial obligation. Using an average consumption of approximately 800 gallons, a customer would be expected to pay close to $3,000.00 during this previous year's sign up period. Another reason is due to our company policies. We do not offer pre-paid options to all of our customers. A pre-paid plan is as much of a liability for our company as it is for the consumer. In a market that is trending upwards a customer can realize a savings by locking in a price lower than future market prices. The opposite is true in a falling market where individuals have locked in at higher prices and due to market disruptions market prices become lower than there locked in price. Historically this has led to consumers resorting to various means to not fulfill their fixed price agreements.
2. **Why waste your time on a program that is only used by so few of your customers?** A pre-paid contract does a few things for an oil company. The main thing it does is it guarantees that the customer will be your customer for the entire heating season and will not resort to price shopping your company against another company. The second thing that it does is it gives a company ratable gallons to be delivered. Due to the fact that our business is weather

dependent certain times of the year are busier than others. By having pre-paid customers that are delivered on an automatic basis one is able to fill in some of the slower days with these deliveries to keep drivers busy and not rely on customers calling in.

3. **Why would a company sell pre-paid oil at a discount to regular deliveries?** The answer to this question lies in the timing of the sale. Pre-paid contracts are often times entered in to during the late spring and early summer months. These sales give oil companies income at some of the slower periods of the year. Summer time is not a high consumption period which can sometimes leave companies struggling for cash flow. Many costs of running an oil company are year round including utilities, payroll, truck payments, financing, and business subscriptions. By selling pre-paid contracts at a fixed markup over the cost of the oil a company is able to increase cash flow during some of the summer months. For example, if a company like mine sells 30,000 gallons at a .50 cent profit, that allows us to utilize $15,000 of profit during some of our slower months to offset some of these summertime costs. In addition many wholesalers are also looking to increase their summer sales and occasionally offer lower pricing during the summer months.

Future of Fixed-Price Contracts:

One thing that I think is important to note is the fact that currently there exist regulations that dictate how oil companies are to protect any pre-paid sales of heating oil in the State of Connecticut. Currently the state requires that we purchase our prepaid gallons using various methods including eighty percent in physical inventory that is delivered, stored and maintained, or the same amount secured by fixed price forward supply contracts. Our other option is to obtain and maintain a surety bond in an amount not less than fifty percent of the total amount of funds paid by consumers.

In light of these requirements I think it is important to note that the companies that have gone out of business resulting in the breach of their pre-paid agreements with consumers did not comply with existing state requirements. Any change to the existing law will not guarantee compliance with the new law. It is likely that additional legislation will lead to further non-compliance by companies that may now comply, because it eliminates the requirement to obtain the fuel prior to selling it to consumers. There is no way to legislate behavior.

I do not support any major changes to the existing law especially one that would require a company to secure a supply bond for eight percent of gallons sold. This change will hurt my business. After discussions with my insurance company it appears that due to the size of my company I will not be able to secure such bonding in turn preventing me from offering prepaid pricing to my customers. It seems that only larger companies will qualify for the bond which will cause an unfair advantage. Bonding is very expensive. Even if I could secure bonding the increased cost would offset any savings I would be able to offer to my customers. Any increase in regulations requires companies to increase compliance. This will increase the cost of doing business. Any additional cost of doing business will in turn be passed down to the end consumer in the form of higher energy costs.

Currently bonding is not a popular option for oil companies due to the difficulty to secure and the high costs associated with the bonds. Even if my company was able to qualify for bonding and felt that the associated costs were reasonable it does not offer me any means to ensure my consumers are protected. A bond only protects the cash value of the consumer's payment. It does not protect the gallon value of a consumer's contract. That is why purchase forward contracts or purchased physical inventory is the best option to ensure the protection of a consumer's investment. In my opinion the legislation is not lacking, however the enforcement is. If the department of consumer protection is not able to enforce current legislation why go through the process to change legislation that will in turn still not be enforced.

Please **oppose HB 5260**, AN ACT CONCERNING HEATING FUEL DELIVERY FEES, CHARGES AND SURCHARGES AND PREPAID GUARANTEED HEATING FUEL PRICE PLAN CONTRACTS.

Thank you.

John Bowman

F.F. Hitchcock

264 Sandbank Road

Cheshire, CT